

# philippine studies

Ateneo de Manila University · Loyola Heights, Quezon City · 1108 Philippines

---

## **Philippine Exporters and the Japanese Market: A Micro Perspective on Philippines-Japan Trade**

Rosalina Palanca-Tan

*Philippine Studies* vol. 55, no. 3 (2007): 373–394

Copyright © Ateneo de Manila University

---

Philippine Studies is published by the Ateneo de Manila University. Contents may not be copied or sent via email or other means to multiple sites and posted to a listserv without the copyright holder's written permission. Users may download and print articles for individual, noncommercial use only. However, unless prior permission has been obtained, you may not download an entire issue of a journal, or download multiple copies of articles.

Please contact the publisher for any further use of this work at [philstudies@admu.edu.ph](mailto:philstudies@admu.edu.ph).

<http://www.philippinestudies.net>

# Philippine Exporters and the Japanese Market A Micro Perspective on Philippines-Japan Trade

This article presents data from 1998 to 2002 on Philippine exports to Japan, particularly on market shares and growth rates. It also provides data on the revealed comparative advantage (RCA) of Philippine export products using 1965, 1975, 1985, 1996, and 1999 data. This article argues that Philippine agricultural, processed food, and consumer manufactures have not been able to fully exploit the potential of the Japanese market due to the inefficiencies of small- and medium-scale enterprises (SMEs), which comprise roughly 90 percent of Philippine exporters. This situation is aggravated by distortionary policies of the Philippine government as well as by insufficient infrastructure and government support. These internal factors make Philippine exporters more vulnerable to stiff competition from China and neighboring Southeast Asian countries, and to the continuing protection and regulation of the Japanese markets.

**KEYWORDS: PHILIPPINES-JAPAN BILATERAL TRADE • PHILIPPINE EXPORTS • JAPANESE IMPORT MARKETS • SMALL- AND MEDIUM-SCALE ENTERPRISES • ECONOMIC PARTNERSHIP**

Philippine exports to Japan continue to lag behind exports to Japan coming from China and other ASEAN countries, the close competitors of the Philippines. In 2001 Japan's imports from the Philippines accounted for just 1.8 percent of Japan's total imports, much lower than Indonesia's 4.3 percent, Malaysia's 3.7 percent, Thailand's 3.0 percent, and China's 16.6 percent. What is preventing the Philippines from partaking of a larger slice of the Japanese market? This is the key question this article aims to address.

There is a dearth of studies dealing particularly with Philippine-Japan trade. Many of the available studies are on Japan's trade with ASEAN countries and with Philippine-Japan economic relations in general. These studies include Valdepeñas (1970, 718–39); Ng, Hirono, and Akrasanee (1987); and Tecson (1996, 318–47). A recent study by Palanca-Tan (2003, 484–508) focuses on Philippine-Japan trade relations in the entire postwar period, providing an in-depth analysis of the critical features and characteristics of these trade relations, particularly in the 1980s and the 1990s. To date, research on trade relations between the Philippines and Japan has been limited to macroeconomic analysis and the use of secondary data. This study seeks to contribute to the existing literature by using primary data and firm-level analysis of the factors that affect Philippine exports to Japan. In addition to official trade statistics, data were collected through focus group discussions (FGDs) and interviews with past, present, and prospective exporters to Japan as well as through interviews with industry leaders and officials of both the Philippine and Japanese governments.

## **SUMMARY DATA ON PHILIPPINE EXPORTS TO JAPAN**

### **Export Product Composition**

Table 1 presents the average annual shares of Philippine products exported to Japan for the years 1998–2002. Semiconductors formed the largest group of export products, accounting for about one-third (33 percent) of all exports. Electronic data processing, which made up for more than a fifth (21.5 percent) of the total, constituted the second largest export product. All electronic products combined accounted for 60 percent of total exports. Machineries and transport equipment parts comprised 8 percent of Philippine exports to Japan, the bulk of which were automotive parts (6 percent).

Food and food preparations contributed 8 percent to merchandise trade earnings from Japan. Slightly over half (4.3 percent) came from exports of

**Table 1. Product share of Philippine exports to Japan, annual average for the years 1998–2002, in percent**

PRODUCT CATEGORY	SHARE
Consumer manufactures	6.38
Food and food preparations	8.01
Processed foods	0.76
Fresh foods	4.34
Marine products	2.91
Tuna	0.52
Shrimps and prawns	1.93
Other marine products	0.46
Resource-based products	6.52
Industrial manufactures	73.36
Electronics	60.24
Components/devices (semiconductors)	33.19
Electronic data processing	21.51
Telecommunications	1.44
Automotive electronics	1.76
Consumer electronics	1.40
Others	0.94
Machineries/transport equipment/apparatus and parts	8.18
Transport equipment	7.07
Others	1.11
Other industrial manufactures	4.94
Special transactions	5.73
<b>Total</b>	<b>100.00</b>

Source: Calculated from DTI 2003

fresh fruits (bananas, pineapples, mangoes, papayas) and vegetables (asparagus, okra, taro). Marine products, mainly shrimps and prawn, accounted for 3 percent. Tuna exports to Japan have been dwindling in recent years, its product share being only 0.5 percent. Nonfood consumer products (e.g., house products, footwear, fashion goods, decorative goods, garments) and resource-based products (e.g., mineral, coconut, and so on) each contributed 6 percent.

It must be noted that electronic product exporters declare their export earnings in two ways. Some declare gross earnings inclusive of the costs of imported raw materials, which account for a substantial portion (more than

90 percent) of the value of the finished product. Others declare net foreign exchange earnings, which reflect the true value-added of the product in the Philippines. Based on industry employment data, industry leaders estimate electronics value-added to be roughly equivalent to only 15 percent of export earnings. Thus, instead of an export contribution valued at US\$3,333 million, the net foreign exchange contribution of electronics in 2002 would be about US\$500 million only, a figure not much higher than the US\$381 million contributed by food products and the US\$268 million contributed by nonfood consumer products.

**Table 2. Growth rates of Philippine exports to Japan and total Philippine exports, annual average for the years 1998–2002, in percent**

PRODUCT CATEGORY	PHILIPPINE EXPORTS TO ALL COUNTRIES	PHILIPPINE EXPORTS TO JAPAN
Total	7.67	5.25
Consumer Manufactures	-1.21	-2.21
Food and food preparations	1.01	-0.82
Processed foods	0.25	-2.78
Fresh foods	4.66	2.97
Marine products	-0.43	-5.11
Tuna	-0.97	-0.10
Shrimps and prawns	2.23	-1.87
Resource-based products	-4.92	-8.32
Industrial manufactures	11.54	8.32
Electronics	14.68	11.51
Components/devices (semiconductors)	13.92	8.30
Electronic data processing	24.33	18.78
Telecommunications	-15.49	38.63
Automotive electronics	9.26	31.55
Consumer electronics	8.30	-11.31
Machineries/transport equipment/apparatus and parts	12.15	3.84
Transport Equipment	11.78	2.65
Automotive parts	11.53	3.18
Special transactions	10.98	9.28

Source: Calculated from DTI 2003

## Export Growth

Table 2 presents the average annual growth rates of Philippine exports to Japan and total Philippine exports for the period 1998–2002. The data show that Philippine exports to Japan have grown much less than total Philippine exports. While overall Philippine exports grew by an average of 8 percent per year during 1998–2002, exports to Japan grew annually by 5 percent only.

The growth of Philippine exports in the period was pulled mainly by industrial manufactures. Growth of industrial exports more than offset the contraction in nonfood consumer goods (-1 percent) and resource-based exports (-5 percent). Food exports, however, managed only a modest an-

**Table 3. Japan's share of Philippine exports, annual average for the years 1998–2002, in percent**

PRODUCT CATEGORY	SHARE
Total	14.63
Consumer Manufactures	8.22
Food and food preparations	30.70
Processed foods	7.04
Fresh foods	60.35
Marine products	35.71
Tuna	16.74
Shrimps and prawns	71.27
Resource-based products	18.02
Industrial manufactures	14.29
Electronics	13.26
Components/devices (semiconductors)	9.91
Electronic data processing	24.11
Telecommunications	33.06
Automotive electronics	28.29
Consumer electronics	15.98
Machineries/transport equipment/apparatus and parts	34.40
Transport Equipment	34.67
Automotive parts	35.43
Special transactions	19.73

Source: Calculated from DTI 2003

nual growth of 1 percent in 1998–2002. This growth was made possible by fresh fruits and seafood exports, which increased by 5 percent and 2 percent, respectively.

The growth rates of industrial exports to Japan were smaller except for telecommunications and automotive electronics, which posted impressive average annual increases of 39 percent and 32 percent, respectively. The contractions in the consumer manufactures and resource-based products were also more pronounced. Furthermore, overall food exports to Japan dropped by 1 percent. The 3 percent moderate growth of exports of fresh fruits was not sufficient to buoy up the whole sector. Exports of processed foods and marine products suffered average annual decreases of 3 percent and 5 percent, respectively.

### **How Important is the Japanese Market to Philippine Exporters?**

As Table 3 shows, Japan absorbed about 15 percent of annual Philippine exports in 1998–2002. Japan was the single biggest buyer of Philippine shrimps and prawns (71 percent), and of fresh fruits and vegetables (60 percent). About one-fourth to one-third of Philippine exports of transport equipment and automotive parts as well as electronic products, such as data processing, telecommunications, and automotive electronics, were destined for Japan. However, Japan had a noticeably lower share of about 10 percent in Philippine semiconductor exports. Even smaller were the shares of Japan in Philippine exports of processed food (7 percent) and consumer goods (8 percent).

## **PHILIPPINE EXPORT NICHES IN JAPAN**

### **Philippine Comparative Advantage**

Ricardo's theory of comparative advantage postulates that a country stands to gain from exporting goods that utilize its abundant resources and importing those that use its less abundant resources. Balassa's index of revealed comparative advantage (RCA) is a quantitative indicator of this comparative advantage. The RCA index of country *j* for commodity *k* is defined as the ratio of the share of country *j* in total world exports of commodity *k* to the share of country *j* in total world exports. An RCA of greater than 1 means that country *j* has a comparative advantage in the production and export of a particular commodity *k*. Conversely, an RCA of less than 1 denotes the absence of comparative advantage.

**Table 4. Philippine revealed comparative advantage (RCA>1), 1965–1999, and Japan's import index (JI), 1999**

COMMODITY/YEAR	PHILIPPINE RCA					JI
	1965	1975	1985	1996	1999	1999
031 fish fresh and preserved		1.09	3.72	2.29	1.37	5.02
032 fish etc. tinned prepared					3.49	4.06
051 fruit fresh nuts fresh dry	1.74	4.34	5.38	2.21	4.02	1.06
053 fruit preserved prepared					3.28	1.64
061 sugar and honey	15.43	17.73	12.05	2.00	1.04	0.59
241 fuel wood charcoal	11.96	8.66	3.86		2.68	2.29
265 veg fiber excl cotton jute	1.03				7.32	0.96
273 stone sand gravel					1.05	0.94
281 iron ore concentrate					2.42	4.78
284 nonferrous metal scrap	4.13	6.69	4.28	1.59	1.36	1.38
285 silver platinum ores					2.03	2.09
292 crude veg materials nes*			1.41	1.37	1.16	1.21
422 fixed veg oil nonsoft	14.32	19.51	14.18	7.88	7.27	0.64
632 wood manufacture nes	7.49	5.82	5.16	1.34	1.26	1.33
666 pottery					1.65	0.83
714 office machine				1.00	4.45	1.09
723 electric distributor machine		6.36	24.58	3.27	3.07	0.80
729 electric machine nes					5.76	0.94
821 furniture			2.74	1.50	1.19	0.94
831 travel goods handbags		3.91	1.04	4.00	3.98	2.64
841 cloth not fur			2.23	3.74	2.02	1.51
864 watches clocks					2.12	1.64
899 other manufactured goods					1.06	1.28
941 zoo animals pets					1.04	1.21

\*nes = not elsewhere specified

Sources: Palanca-Tan (2003, 504), Appendix I-B for RCA 2-digit Standard International Trade Classification (SITC), 1965 to 1996; Palanca-Tan (2004, 6–7), Tables 4 and 6 for 1999 RCA and JI 3-digit SITC

Table 4 reveals that throughout 1965 to 1999 the Philippines maintained a comparative advantage for fruits; sugar and honey; fuel wood charcoal; metal ores and scrap; fixed vegetable oil and fats; and wood manufactures. Fresh and canned fish; semiconductors and other electronic components; and travel goods and handbags reflected high RCA values starting from the mid-1970s. Comparative advantage in furniture and clothing was achieved



in the mid-1980s. Only in the 1990s did the Philippines start to reveal a comparative advantage in pottery, office machines, watches and clocks, and zoo animals and pets.

To identify which among the Philippine products with comparative advantage have an export potential in Japan, we look at the RCA-equivalent index for imports, referred to in this study as the import index. The import index of country *j* for commodity *k* is the share of country *j* in total world imports of commodity *k* to the share of country *j* in total world imports.

Japan's import index (JI) indicates the product needs and wants of the Japanese market that are sourced externally (products with JI of greater than 1). The last column of Table 4 reveals that of the twenty-four commodities for which the Philippines has a comparative advantage, sixteen have a JI greater than 1. These are fish, fruits and nuts, fuel wood, metal ores and scrap, crude vegetable materials, wood manufactures, office machines, travel goods, clothing, watches, and zoo animals and pets.

## **The Philippine Position in Japan's Markets**

The RCA and JI indices presented above indicate what the Philippines can potentially export to Japan. To look at how Philippine exports fare in the Japanese market, we adopt the approach used by the World Bank to classify Philippine export products to Japan according to four quadrants in a Market Position Matrix: Optimal Quadrant (I), Lost Opportunity Quadrant (II), Vulnerable Quadrant (III), and Retreat Quadrant (IV).

A product is considered dynamic (or stagnant) if its share in the total imports of Japan is increasing (or decreasing). A Philippine export product in Japan is considered competitive (or noncompetitive) if the Philippine share in Japan's market is growing (or falling). An "optimal" market position (I) is one where the Philippine market share in Japan's dynamic import goods is increasing. The quadrant of "lost opportunity" (II) is a situation where the Philippines loses its market share in Japan's dynamic imports. The "vulnerable" position (III) for the Philippines suggests an increasing share in Japan's stagnant import products. Finally, the "retreat" quadrant (IV) is a situation where the Philippines is not competitive in Japan's stagnant import goods.

Philippine-Japan trade data from 1996 to 2000 (the four-digit SITC) are used to categorize Japan's import goods into dynamic and stagnant, and Philippine export products into competitive and noncompetitive. The majority—or almost three-fourths—of the product items in the optimal quad-

rant of the Philippines's Japan Market Position matrix includes electronics, automotive, and other industrial manufactures (circuits, resistors, capacitors, switches, radio receivers, input-output units, and so on). Only a few agricultural products (namely, fresh and dried bananas, dried and salted fish) and consumer manufactures (e.g., curtains and other furnishings, babies' garments and clothes, knitted garments, wood furniture, trousers, t-shirts, and vests) are in the optimal quadrant.

There is a preponderance, however, of agricultural and food products (e.g., other fresh and dried fruits, fresh and chilled vegetables, sugar confectionary, fermented beverages, frozen fish fillets, prepared crustaceans and mollusks, sauces/seasoning/condiments, frozen fruits and nuts, unpickled vegetables, sausage of meat, frozen vegetables) as well as consumer manufactures (e.g., festive articles, suits and ensembles, clothing accessories, plastic articles, suits/jackets/trousers, pulp/paper/board articles, plastic floor and wall covering, plastic and rubber apparel, children's toys, metal furniture, glass articles, skirts and divided skirts, textile articles, nightwear and underwear, household linens, mattresses, knitted hosiery, hand paintings, and drawings) in the "lost opportunity" quadrant.

The Philippine comparative advantage in semiconductors and other electronic machine parts, therefore, appears to be gaining some grounds in the Japanese market. However, despite some comparative advantage of the Philippines in agricultural, food, and consumer manufactures, these Philippine products have not performed well in the Japanese market. The remainder of this article attempts to address two issues. The first is to uncover the reasons behind the failure of Philippine agricultural, food, and consumer product exports to successfully compete in the growing import markets of Japan. The second is to look at the factors that may enable the Philippines to reap the full benefits that can be derived from the optimal market position of its electronic parts and other industrial manufactures in the Japanese market. These two tasks are done through an analysis of the Strength, Weaknesses, Opportunities, and Threats (SWOT) of Philippine exporters, which are grouped into two: (1) exporters of agricultural products, food, and other consumer goods that dominate the lost opportunity quadrant, and (2) exporters of industrial manufactures, mainly electronic and automotive parts and accessories, that lead the optimal quadrant. The next two sections present the results of the SWOT analysis.

## **AGRICULTURAL, FOOD, AND OTHER CONSUMER GOODS**

The Japanese market for imported agricultural products, food, and other consumer goods is expanding and offers business opportunities to Philippine exporters in view of the comparative advantage of the Philippines in these product items. However, there are also a host of obstacles in tapping these opportunities. Production inefficiencies and cost disadvantages constrain Philippine exporters in overcoming these obstacles.

### **Opportunities in the Japanese Market**

**Agricultural and Food Products.** The Philippines grows the principal fruit items that Japan imports: bananas (58 percent of Japan's total fruit imports), pineapple (7 percent), mango (1 percent), avocado (1 percent), and papaya (1 percent). The Philippines is Japan's major source of tropical fruits, supplying the market 79 percent of its bananas, 98 percent of its pineapples, 61 percent of its mangoes, and 48 percent of its papayas (JETRO 2002c). Pineapple accounts for 12 percent of Japan's import of fruit juices and the Philippines is the dominant supplier, with a 36 percent market share (*ibid.*, chap. I.6).

The present share of the Philippines in Japan's vegetable imports of just 1 percent leaves much room for expansion.<sup>1</sup> The two major fresh vegetable exports of the Philippines to Japan are okra and asparagus. Okra fetches a price advantage as demand comes from hotels and restaurants and, hence, is price inelastic. Another vegetable export to Japan is frozen taro with a market share of only 0.2 percent, a far second to China's 99.8 percent (*ibid.*, chap. I.10). Philippine pumpkin, in frozen form, is also a potentially exportable vegetable to Japan.

As the Japanese become increasingly health conscious, the traditional requirements for appearance and size of vegetables are replaced by safety considerations, such as organic or chemical-free vegetables. The present miniscule share (2 percent) of the organic market in Japan is expected to expand rapidly in the next few years. Consultants of Japan External Trade Organization (JETRO) see a niche for Philippine growers in the organic market, particularly onions (28 percent of vegetable imports of Japan) and carrots. According to Japanese experts, these two vegetables can be cultivated in the Philippines cheaply and easily without the use of chemicals.<sup>2</sup>

The upward trend in Japan's fruit and vegetable imports brought about by the vigorous market liberalization efforts in the 1990s is expected to continue for the following reasons: (1) the persistent decline in domestic pro-

duction, given the shrinking farming population (as aging Japanese farmers are not replaced by younger ones), (2) the sourcing of out-of-season supply (e.g., pumpkin) from countries with growing seasons different from Japan's, (3) the diversification of vegetable imports due to changing culinary tastes, and (4) the growing use of reefer containers in marine transport that makes possible the importation of large volumes of fresh vegetables (*ibid.*).

Furthermore, relative to its Southeast Asian competitors, the Philippines is a nearer source of Japan's marine product imports such as tuna and exotic seafood items. Japan is the world's largest market of raw tuna for sashimi. Since Japan's domestic catch of tuna is sluggish, the share of imported tuna in the Japanese market is gradually increasing. In 2000 58 percent of tuna supply in Japan was imported. Shrimps and lobsters as well as crabs are the other leading imported seafood products in Japan, with farmed black tiger accounting for an overwhelming 96 percent share of the market in shrimps and lobsters. For medium- and large-size shrimps, imports have a market volume share of more than 98 percent. The share of imported crabs is about 75 percent (*ibid.*, chap. I.19).

**Nonfood Consumer Products (Apparel and Fashion Goods, Household Goods, Furniture).** As an offshoot of Japan's economic slowdown in the 1990s, demand for luxury-class branded products from Europe and the United States flattened, and lower priced imports from China and Southeast Asian countries have become increasingly popular. Asian-made consumer products target the mass market and medium-quality categories in Japan's market. Mass market items usually involve consignment processing and are manufactured with the abundant materials available in China and Southeast Asia. Medium-quality items are imported in small-sized lots with a large variety of designs; they require shorter delivery times (*ibid.*, chap. II.3). Given that Philippine production costs are already high relative to China, Vietnam, and Indonesia, Philippine exporters can focus on medium-quality items because the country's advantage lies in product design, craftsmanship, and the use of indigenous materials.

Apart from favorable demand conditions in Japan's consumer goods markets, other market premiums exist. One is a price premium. Relative to other foreign buyers, the Japanese market is less price-conscious, with a willingness to pay more for as long as quality goods are obtained. A second premium is the assistance extended by Japanese buyers to enable exporters to meet the requirements of their market. This assistance includes regularly inspecting plants, developing tools and equipment to increase productivity, and provid-

ing equipment and machineries on credit. A third premium is the loyalty of Japanese buyers, who will not seek and will not accept offers from other suppliers for as long as their present suppliers satisfy all their requirements.

## **Protection and Selectivity of the Japanese Market**

Although the opportunities offered by the Japanese market are many, there are hurdles in tapping them. Despite recent trade liberalization programs, Japan persists in using the food self-sufficiency argument to justify the continuing protection and regulation of its agricultural and food sectors. Tariff peaks still exist for agricultural products. Even with the generalized system of preferences (GSP), Japan's tariff rates on agricultural products are still high: 10 percent for fresh bananas, 17 percent for fresh pineapples, 5.5 percent for banana chips, 15–21.2 percent for *nata de coco*.<sup>3</sup> Japan also continues to impose quantitative restrictions on fisheries products, which are justified on the basis of sustainable resource use.

In addition to tariff and import quota barriers, access by foreign firms to the Japanese market remains difficult and very costly, as the distribution system stays complex, multilayered, nontransparent, and dominated by exclusive relations among producers, wholesalers, and retailers. Hence, successful Philippine exporters of agricultural goods to Japan are limited to the big farming conglomerates, such as Dole Philippines, and some Japanese-managed farms. Moreover, penetrating Japan's nonfood consumer goods market is capital-intensive. It requires regular attendance in trade fairs and exhibits, and frequent visits to shops and markets inside and outside Japan, a highly expensive marketing approach that small-scale Philippine consumer goods exporters cannot afford.

Furthermore, there are nontariff barriers. The sanitary and phytosanitary (SPS) conditions and quarantine regulations of the Japanese market (e.g., standards on food additives and residual agricultural chemicals in the Food Sanitation Law) are said to be the most complex and stringent in the world, and the biggest impediment for agricultural and foodstuff exporters to Japan. Particularly cited in the FGDs and interviews of exporters are: (1) Japan's metabisulfide<sup>4</sup> standard of 50 parts per million (ppm),<sup>5</sup> (2) the required vapor heat treatment (VHT) for fresh fruits, and (3) numerous qualitative standards for food and other consumer products, mostly factors that do not constitute health and safety risks as defined by the WTO SPS agreement. Exporters are distressed over the numerous—in terms of both number of

cases and volume of goods—claims concerning product quality and conditions made by Japanese buyers, and there is no system to verify and refute the validity of those claims.

## **Competition**

Although the Philippines has the dominant market share for the fruit items that it exports to Japan, it cannot be complacent with the competition posed by Ecuador and Taiwan for bananas, Mexico for mangoes, and Hawaii for papaya. In trying to increase its vegetable exports to Japan, the Philippines has to contend with China, which already has gained dominance over several of the Japanese vegetable markets and overtaken many of the longtime major Japanese suppliers such as the United States. China can sell larger volumes at much lower prices than the Philippines. For fresh and frozen seafood exports, such as shrimp, prawns, and tuna, the closest competitors of the Philippines are Thailand, Indonesia,<sup>6</sup> and Vietnam.

In the case of nonfood consumer goods, the main pressure comes from China. Its abundant supplies of raw materials, low wages, and competitive prices, helped further by considerable technical assistance from Japan, have made it the leading supplier—accounting for more than half of imports—of the Japanese consumer goods market in almost all product categories. Not only Japanese makers but European and U.S. firms supplying the Japanese market have also transferred their production facilities to China to reduce costs and shorten delivery time. Support industries for these sectors are emerging and growing rapidly in China as well. Fast becoming a major player to trail China and overtake other Southeast Asian countries is Vietnam, which is now next to China and ahead of Thailand and Indonesia as source of apparel exports to Japan.

The Philippine advantage in design and craftsmanship in nonfood consumer products easily fades with certain, although disagreeable but nevertheless common, business strategies of importers. Foreign buyers buy samples or take photographs of Philippine-made products during trade fairs and exhibits, and subsequently have these products copied by factories in China. The Philippine advantage in goods made from materials that are only available here is likewise easily lost with the exportation of unprocessed raw materials. This is the case for raffia, a soft natural fiber obtained from *Raphia* palm leaves and used for weaving, winding, and making baskets and mats, which the Philippines is now exporting to China.

## **Philippine Noncompetitiveness**

Because many Philippine consumer goods exporters are small- and medium-scale enterprises (SMEs), there are numerous sources of cost disadvantage. One is deficiency in technological know-how. Simple heat insulation technology to conserve energy, surprisingly, is still unknown or not applied in many of the country's small- and medium-scale firms.<sup>7</sup> A major contributory factor to this problem is the absence of linkages and cooperation between the private sector and academic and research institutions. The SMEs do not have the capacity to engage in their own research and development programs, but have to rely on outside pools of technical expertise and facilities for information on efficiency-enhancing technologies and for product and raw materials development experimentations. The absence of economies of scale, particularly for major cost items in export production such as packaging,<sup>8</sup> storage, and shipping/transportation is another source of cost problems for SMEs.

The insufficiency of credit facilities for collateral-constrained SMEs is also disadvantageous to the exporters. Most of them still rely on the short-term Packing Credit Line for both short-term and long-term capital needs. The problem of short-term credit used to finance long-term requirements for fixed capital acquisition is well-known. When the supply of funds dries up, loans are not rolled over and SMEs run out of money to finance their daily operations. Some exporters resort to informal financial markets, where cost of capital can be as high as 20 percent per month.<sup>9</sup>

Furthermore, certain government policies tend to raise the costs shouldered by exporters. These policies include those on the minimum wage, indiscriminate trade liberalization (e.g., exports of unprocessed raw materials), inadequate infrastructure programs (communication and transportation), and the regulation of sugar imports (a major ingredient in food exports). Apart from these competitiveness-impairing policies, the Philippine government does not provide sufficient leadership and support for industry and export organizations in the field of food and consumer manufactures. This situation is in sharp contrast with other Southeast Asian countries where government leadership and initiative in export promotion are clearly evident in international trade fairs and exhibits,<sup>10</sup> international business meetings and gatherings,<sup>11</sup> and in the commercial and marketing "intelligence" activities of the trade sections of their overseas diplomatic missions.

Tuna canning (and exports of marine products, in general) provides us a classic example of Philippine exporters' noncompetitiveness. Despite the

greater proximity of the Philippines, compared with its Southeast Asian competitors, to both supply (tuna) and demand (Japan), the Philippines is losing the race to Thailand, Indonesia, and recently to Vietnam. Philippine tuna canners admit that, in terms of technological know-how, they lag behind their Thai counterparts.<sup>12</sup> Philippine tuna canners suffer from cost disadvantages in shipping, storage, and packaging because of their smaller size.<sup>13</sup> The industry also does not receive the government support enjoyed by its Thai, Indonesian, and Vietnamese<sup>14</sup> counterparts.

## **INDUSTRIAL MANUFACTURES**

Philippine exporters of electronics and automotive parts and accessories are relatively more successful in taking advantage of the recently growing Japanese import market, as indicated by the optimal market position of these Philippine export products in Japan. However, some problems exist the most critical of which is the limited impact of this export success on the Philippine economy due to the absence of forward and backward industry linkages.

### **Opportunities in the Japanese Market**

**Electronics.** Of the 60 percent share of electronics in total Philippine exports to Japan, more than half is comprised of components and devices such as discretes, integrated circuits (ICS), power transistors, signal transistors and diodes, micro controllers, and so on, collectively referred to as semiconductors.

The growth of the global semiconductor market accelerated in the latter part of the 1990s due to major technological breakthroughs in audiovisual, computer, and telecommunications systems. From 1999 to 2000 the market expanded by more than 35 percent, with Japan accounting for more than a fifth of the global market. Its semiconductor market likewise grew by 35 percent due specifically to brisk demand for cellular phones, personal computers, digital cameras, and digital television. The global slowdown in demand for electronic products in 2001 resulted in a decrease in the demand for semiconductors. However, the Japanese semiconductor market showed more vitality as it posted a contraction of only 6 percent, much smaller than the 35 percent worldwide decline. The Japanese market quickly recovered in 2002, and is expected to expand further as an offshoot of new demand for next-generation cellular phones; televisions and set-top boxes for household use; video game units; and higher speed, larger capacity data communica-



tion services and other telecommunications infrastructure. These types of equipment require semiconductors loaded with technologies for communication networks and image processing (JETRO 2002a).

**Automotive Parts and Accessories.** In August 1995 Japan deregulated the importation of automotive parts and accessories. Since then several measures to promote imports have been undertaken. First, JETRO actively assists and supports sales promotion missions in Japan for foreign auto parts suppliers as well as overseas auto parts buying activities of Japanese companies. The JETRO has also created permanent exhibition facilities for foreign-made parts at imported automobile showrooms in Tokyo, Nagoya, and Osaka. In addition, the Japan Federation of Auto Parts Sales Association has put up a consultation window for foreign auto parts manufacturers planning to enter the Japanese market. Finally, the Japan Automobile Service Promotion Association has developed an information network system on foreign auto repair parts. The system includes a database on types, prices, and other detailed information on foreign parts manufacturers, who can register via the association's home page or by mail to be included in the database. As a consequence, the value of imported assembly and replacement auto parts and accessories increased by 124 percent and the share of imports in the sector increased by 24 percent from 1995 to 1996, despite the decline in overall industry sales (JETRO 1998, 3–4).

Another recent development that works well for imports is the diversification in the sourcing and distribution of replacement auto parts and accessories. In the past suppliers were limited to producers of genuine parts and recommended parts.<sup>15</sup> Now imported parts (those supplied directly from auto part manufacturers), private brand parts of auto parts dealers, parts supplied by used cars dealers, and salvaged parts are available in the market. While genuine parts still dominate the replacement parts market, imported ones are making substantial inroads for common parts and accessories, such as spark plugs, wiper blades, brake pads, air filters, oil filters, and clutches (*ibid.*, 5).

In particular, nationwide auto parts store chains led by Autobacs and Yellow Hat as well as local independent stores are increasingly becoming popular. These stores have resorted to foreign products not only as a strategy to reduce cost but also to differentiate themselves from their competitors. Although these stores go to Europe and the United States for name brand products, they source their own private brand products and bargain items from Southeast Asia (*ibid.*, 15, 18).

## **Sectoral Advantage**

The major strength of the Philippine industrial sector comes from the skilled, highly literate, and English-speaking labor force. The industrial sector also receives relatively greater government support than other sectors. Most of the exporting companies are large enterprises with little or substantial foreign capital infusion, are located in the export processing zones, and enjoy tax incentives. Largely because the sector is the biggest contributor to the country's exports earnings and because of the presence of large and multinational players in the sector, government has been more receptive to the sector's calls for less red-tape. Paperless trading, including custom procedures, for instance, has already been set up and implemented for some electronics and automotive industries.

## **Competition**

The major threat to Philippine exporters of electronics, auto parts, and other industrial manufactures comes from competing Asian countries. Even for industrial manufactures, China is fast becoming the production bases of Japanese firms, with nearly half of Japanese foreign direct investments (FDI) in electronics now going to China. Following China as site for Japan's FDI is Vietnam. Since its reorientation toward a market economy, Vietnam has been very aggressive in attracting foreign investors. Vietnam was among the first countries (together with the U.S., Germany, and other European countries) and the only Southeast Asian country visited by the JETRO-sponsored auto parts and accessories buying missions from 1995 to 1998 (*ibid.*, 19).

## **Philippine Constraints**

The electronics and automotive industries in the Philippines rely largely on assembly-line operations. Labor, the country's value-added in this sector, only covers a small portion (roughly 10 percent) of the assembled product. The greater part consists of imported raw materials, most of which are supplied by the foreign buyer.<sup>16</sup> Hence, the substantial contribution of these industries' exports in gross terms becomes insignificant in net terms. Based on employment data, industry leaders estimate the net foreign exchange earnings of the electronics industry to be only about 15 percent of reported exports. This rough estimate is consistent with Morisawa and Tecson's (1997, 84) survey, which reveals a local content of 10 percent for the electronics as-

sembly industry, and 15–20 percent for the automotive industry. Their study attributes the low local value-added partly to the dominance of multinational corporations, which they say are less inclined to establish linkages with local suppliers (*ibid.*, 79).

Moreover, a central reason for the high degree of import dependence of the electronics and automotive industries, in general, is the weak and underdeveloped state of support industries. There have not emerged enough firms in the Philippines that can supply the raw materials needed by electronics and automotive exporters, for reasons that have been discussed extensively by Morisawa and Tecson (1997). Their explanations focus on the difficulties encountered by supplier firms, which are mostly SMEs: (a) fluctuations in orders, (b) lack of access to raw materials and capital equipment, (c) high risk of capital and technological investment, and (d) financial constraints. Government policies aimed at developing the support industries have also failed. The Electronic Local Content Program (ELCP) of 1975, for instance, only created a captive market of assemblers for the supplier firms. Given the protective environment, firms were not induced to upgrade quality and be cost-effective (*ibid.*, 92). The numerous financing programs (numbering more than thirty) put up by the government for the electronics SMEs likewise did not address these firms' problem of insufficient collateral—the biggest constraint to credit access. The results of these financing programs were also limited as they were not disseminated properly and were not focused on capital expenditures for productivity improvements and technological upgrading (*ibid.*, 90–93).

A second major area of concern for this sector relates to country risk factors—peace and order condition, political stability, and policy continuity. The industrial manufacture export sector, being highly capital-intensive, is the most sensitive to country risk factors. Given considerable uncertainty in the business and policy environments, both domestic and foreign firms are discouraged to invest huge sums of money that are required by the sector.

Despite the greater attention the industry is receiving from the government relative to other sectors, there is still a perceived lack of government support. Industry players call for the government to provide better infrastructure (e.g., land and air transportation infrastructure) and to establish a performance monitoring system for government agencies that will significantly reduce, if not eliminate, red-tape and corruption. The mere size and global exposure of the industry make it susceptible to even the slightest changes in the regulatory environment.

Another factor that holds back the industry is the limited cooperation between industry and academic institutions. The industry requires a highly and appropriately trained manpower. Many of the engineering and vocational program curricula in the Philippines, however, are either irrelevant or inadequate. The educational and other training institutions in the Philippines also lack facilities for practical training. The government has failed to provide the assistance required by learning and training institutions, and to facilitate the interaction between industry and academe.

## **CONCLUSION**

In examining firm-level factors that affect Philippine exports to Japan, this article first identified Philippine products that possess export prospects in Japan, and then conducted an analysis of the strengths and weaknesses of these production sectors as well as the opportunities and threats that they face. The analysis revealed that the inability of Philippine agricultural, processed food, and consumer manufactures to successfully tap the growing import markets of Japan can be traced largely to: (1) low quality and price competitiveness arising from insufficient technical know-how, lack of economies of scale, and lack of credit facilities for SMEs, which comprise roughly 90 percent of the exporters; (2) certain distortionary government policies; and (3) insufficient infrastructure and government support. Apart from these domestic factors, there is severe competition from China, Thailand, Indonesia, and Vietnam. At the same time, there remains the protection and regulation of the Japanese markets.

In line with the Japan-Philippines Economic Partnership Agreement, to enable existing and prospective Philippine exporters to fully exploit the potential of the Japanese market the following may be necessary: (a) the complete opening of Japan's agricultural and processed food sectors to the Philippines; (b) import promotion programs, particularly for Philippine-made products; and (c) SME-focused efficiency enhancement training programs and capital accumulation loan programs. Further, the benefits that the Philippines can reap from the optimal position of its electronics and automotive parts exports in Japan may be enhanced if support industries develop in the Philippines, a development which requires, among other things, Japanese assistance for human resources development programs.

## Abbreviations

<b>DTI</b>	Philippine Department of Trade and Industry
<b>FGD</b>	focus group discussion
<b>GSP</b>	Generalized System of Preferences
<b>JETRO</b>	Japan External Trade Organization
<b>JI</b>	Japan's import index
<b>PIDS</b>	Philippine Institute for Development Studies
<b>RCA</b>	revealed comparative advantage
<b>SITC</b>	Standard International Trade Classification
<b>SMEs</b>	small- and medium-scale enterprises
<b>SPS</b>	sanitary and phytosanitary
<b>SWOT</b>	strengths, weaknesses, opportunities, and threats

## Notes

*This article is a short version of PIDS Discussion Paper Series No. 2004-10 titled "Prospects and problems of expanding trade with Japan: A survey of Philippine exporters," a research project funded by the Philippine APEC Study Center Network (PASCN) at the PIDS.*

- 1 Notes from the JETRO Workshop Series on Vegetable Production/Marketing for Japan, held in Makati in July 2003.
- 2 The Philippines used to export onions to Japan in the 1990s. Philippine onions satisfied the quality requirement (juicy and soft) but failed to meet the size requirement. Lecture given by Mr. Takusari at a JETRO Manila workshop held in May 2003.
- 3 These tariff rates were cited by the Japanese importer-customer of a major Philippine food exporter to Japan. These figures were double-checked against those in the various tariff tables in JETRO 2002c.
- 4 Metabisulfide is a chemical preservative to prevent the growth of microorganisms and subsequent spoilage. It is also an antibrowning agent.
- 5 Japan's figure is too low compared with the 1,000 ppm of Europe and the 200 ppm of the United States.
- 6 Completing the list is India. The Philippines is not included in the list of top five apparel exporters to Japan, despite the fact that Thailand, Indonesia, and the Philippines were the Southeast Asian countries that first stepped in to take the place of Korea and Taiwan in the late 1980s as apparel exporters to Japan.
- 7 During the FGD with directors and members of Philfoodex, one food processor mentioned how her firm's monthly electricity bill had gone down by about P25,000 after following an advise by a JICA consultant to install a heat insulation system, which cost the firm a one-time outlay of about P9,000 only.

- 8 Domestically sourced packaging materials are more expensive than imported ones. Importation, however, would require volume.
- 9 Interview with a Philfoodex director.
- 10 In such fairs and exhibits, Philippine booths are observed to be so inferior to booths of other Asian countries.
- 11 In these international business meetings and gatherings, the country's Asian competitors would come with a unified stand due to strong industry/export organizations supported by their respective governments.
- 12 Thai tuna canners can fill up a tuna can and do it nicely, using less raw material (tuna) than Philippine tuna canners.
- 13 Thailand's biggest tuna canner is bigger than all tuna canners in the Philippines combined.
- 14 For instance, Vietnamese firms, in partnership with their government, have even developed a boat building industry in support of the growing fishing industry in Vietnam.
- 15 Recommended parts are nongenuine auto parts that are approved by the Japan Automobile Products Association.
- 16 Two models are employed in these sectors. For model 1, buyers supply the assembler/exporter all the major raw materials. For model 2, also referred to as "turnkey," the assembler/exporter sources raw materials on its own.

## References

- Bureau of External Trade Promotions, Department of Trade and Industry (DTI). 2003. Tradeline Philippines: Statistics. Internet database, <http://tradelinephil.dti.gov.ph>, accessed 27 July 2003.
- Japan External Trade Organization (JETRO). 1998. Japanese market report—regulations and practices: Automotive parts and accessories. Mimeographed. Tokyo: JETRO.
- . 2001. Japanese market report—regulations and practices: Household products. Mimeographed. Tokyo: JETRO.
- . 2002a. Japanese market report—regulations and practices: Electronic components. Mimeographed. Tokyo: JETRO.
- . 2002b. Japanese market report: Canned fish and seafood products. Internet document, <http://www.JETRO.go.jp/ec/e/market/jmr/063.html>, accessed 27 July 2003.
- . 2002c. *JETRO marketing guidebook for major imported products*. Tokyo: JETRO.
- Morisawa, Keiko and Gwendolyn R. Tecson. 1997. Japan's role in the development of support industry in the Philippine electrical and electronics industry. In *Image and reality: Philippine-Japan relations towards the 21st century*, ed. Rolando S. Dela Cruz, 75–110. Quezon City: Institute of International Legal Studies, University of the Philippines Law Center.
- Ng, Chee Yuen, Ryokichi Hirono, and Narongchai Akrasanee. 1987. *Industrial restructuring in ASEAN and Japan*. Singapore: Institute of Southeast Asian Studies.
- Palanca-Tan, Rosalina. 2003. Postwar trade. In *Philippines-Japan relations*, ed. Ikehata Setsuho and Lydia N. Yu-Jose, 484–508. Quezon City: Ateneo de Manila University Press.

- . 2004. Prospects and problems of expanding trade with Japan: A survey of Philippine exporters. PIDS Discussion Paper Series No. 2004-10. Makati City: PIDS.
- Tecson, Gwendolyn. 1996. Desiderata for future Philippines-Japan economic relations. In *Towards a shared future through mutual understanding: Proceedings of the first international conference on Philippines-Japan relations*, 318–47. Manila: De La Salle University Press.
- Valdepeñas, Vicente. 1979. Japan in postwar Philippine economy. *Philippine Studies* 18(4): 718–39.
- World Trade Organization (WTO). 1998. *Trade policy review: Japan 1998*. Geneva: WTO.